UNITED STATES DEPARTMENT OF COMMERCE
The Under Secretary for International Trade
Washington, D.C. 20230

CONFIDENTIAL

January 25, 1982

MEMORANDUM FOR: Robert McFarlane
Lawrence S. Eagleburger
Fred C. Ikle
Richard D. DeLaurer
Robert D. Hormats
Norman Bailey

FROM: Lionel H. Olmer

The attachment is an attempt to clarify pending issues on export control vis-a-vis efforts to delay the Siberian pipeline. Your views are requested as soon as possible.

Although the facts and policy implications are accurately described (in brief), there remains a question of whether legal authority exists to control foreign made products of U.S. technology which was transferred prior to imposition of the expanded sanctions (December 30, 1981). Our General Counsel, Sherman Unger, will coordinate with GC's from other Departments to more thoroughly address this issue.

Attachment

cc: Sherman Unger

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UNCLASSIFIED UPON REMOVAL OF ATTACHMENT

Not referred to DOC

ECONOMIC SANCTIONS
ISSUES RELATING TO EXTENSION OF OIL AND GAS CONTROLS

Introduction

The President announced sanctions on December 29, 1981 against the USSR that broadened oil and gas controls to include refining and transmission equipments. The controls prevent the export or reexport of U.S. origin commodities and technology to the USSR. Commerce Department specialists maintain that the broadened controls require additional extension to block or delay the construction of the West Siberian Pipeline. The proposed extensions are:

I. Barring of all "U.S. Persons" (controlled foreign subsidiaries of U.S. corporations) from exporting oil and gas equipments to the USSR regardless of U.S. content, and

II. Barring the export to the USSR of foreign products based on U.S. technology without U.S. components.

By further extending the controls, the U.S. will have a significantly higher probability of delaying or blocking the pipeline; our allies are expected to object strongly, however. New controls would also blunt criticism by the press and the AFL-CIO. On the other hand, these extensions could cause long-term US business losses as foreign customers turn in the future to non-US suppliers of technology and components. Decisions need to be taken regarding the extension of the new controls.

Two other issues have surfaced since December 30th. Several foreign governments (U.K., FRG, and Italy) and companies have informally requested that signed contracts should not be affected by the sanctions and that components already shipped from the U.S. should not require reexport authorizations. Turbine rotors supplied by G.E. to firms in Western Europe are affected by both these issues. Several hundreds of millions of dollars and thousands of jobs are involved. Decisions should be taken on how to handle requests by governments to make exceptions to our sanctions.

Present Coverage

The expanded controls cover:

- Exports or reexports of U.S. origin goods (regardless of physical location)
- Products of technology exported after December 30, 1981
- Reexport of foreign produced commodities containing U.S. origin components

Issues for Decision

I. Should the U.S. prevent U.S. foreign subsidiaries from selling controlled commodities?

Legal Authority: Legal authorities exist under the EAA to assert control over U.S. subsidiaries.

Discussion: Although authority exists to control subsidiaries, it has been used only once (Levi's uniforms for the Moscow Olympics). If this action is taken, the major contracts affected include Dresser Industries' French subsidiary ($30 million contract for the sale of 21 compressors) and Howmet Turbine Components Corporation's U.K. and French subsidiaries ($4 million contract under negotiation). This option provides the President significant leverage to delay or even block the pipeline. Allied reaction is expected to be strong but this step is necessary if we are to stop compressor sales. It may be possible to get voluntary allied cooperation to prevent sales of relevant equipment. Voluntary compliance should be discussed before action is taken.

Decision: Include all U.S. foreign subsidiaries under the sanctions (consult with allies to solicit voluntary agreement before actually implementing.)

Yes _____ No _____

II. Should the U.S. assert control over foreign made products of U.S. technology which was transferred before December 30, 1981?

Legal Authority: No precedent exists under the export regulations for such an application (Carter Administration controls on oil and gas production and exploration equipment were applied prospectively). It can be done, however; but on tenuous legal grounds.

Discussion: Several companies in Europe use General Electric's technology to produce gas turbines, and have signed contracts with the USSR to supply the pipeline's 41 compressor stations. No deliveries have been made. At the time of the technology transfers, no license nor written assurances were required. The G.E. Manufacturing Associates include AEG-KANIS Turbinehfabrick (West Germany), John Brown Engineering (U.K.), and Nuovo Pignone (Italy). Alsthom-Atlantique (France) also has a license arrangement with G.E. to produce turbines. Lastly, Rolls Royce (U.K.) manufactures a turbine for which a coupling shaft is a product of U.S. technology, as is the compressor itself.

If these products could be prevented from going to the Soviet Union and option I is implemented, the President would be provided significant leverage to delay or block the pipeline. The allies argue that we should only include products of U.S. technology which is transferred after December 30, 1981, and that to cover earlier technology is retroactive application of U.S. law.

Decision: Include in our sanctions foreign-made products of U.S. technology which was transferred before December 30, 1981? (Consult with Allies to solicit voluntary agreement before actually implementing.)

Yes _____ No _____

III. Grant reexport authorization for controlled components already in Europe?

Legal Authority: The EAA and present regulations clearly require a reexport authorization from Commerce

Discussion: Over the past two years, G.E. and other companies have exported to Western Europe components that didn't require the government's prior approval but that now require a validated license because of the sanctions the President imposed on December 30th. For example, John Brown has 6 rotors, AEG Kanis has 2 rotors, and Nuovo Pignone 14. Each rotor costs $1.5 million. Ambassador Louis has suggested granting these authorizations to ease tensions between the U.S. and our allies, since without the U.S. rotors the companies would lose over $500 million in business (some of which would be covered by insurance) and result in substantial layoffs. The situation is especially acute in the U.K.

By granting this exception, the ultimate fate of the pipeline will not be affected. The pipeline requires 125 turbines and this would allow only those currently in Europe (22) to be sent to the U.S.S.R. Rotors for the rest of the turbines would require export licenses to leave U.S. shores. Granting an exception, however, could be used as a bargaining chip to induce allies to take independent steps to stop the pipeline. This action would be viewed as a dilution of the sanctions that were imposed on December 30th.

Decision: Grant exception by issuing reexport authorization while negotiating with allies for them to take independent steps to delay the pipeline.

Yes_____ No_____

IV. Grant export Licenses to G.E. to export 103 rotors to fulfill present contracts?

Legal Authority: EAA and present regulations clearly require validated licenses to export turbine rotors.

Discussion: Contracts or Letters of Intent (Nuovo Pignone) exist to sell 125 gas turbines for the pipeline. G.E. will supply the rotors while final assembly will be in the U.K., FRG, and Italy. With U.S sanctions, the rotors can't be supplied thereby preventing the foreign companies from delivering over $500 million of turbines. Substantial lay-offs would result, especially in the U.K. The respective governments are expected to request exceptions to the sanctions. While alternatives to G.E. gas turbines exist, they are either less reliable, more costly or impractical. Granting the exceptions would be viewed as substantially diluting the sanctions imposed on December 30th and invite criticism in the press. Agreeing to this option would ensure that the pipeline is built.

We could, however, use an exception for present contracts to entice our allies to take independent actions (withdrawal of loan guarantees) to delay or block the pipeline. The negotiations, if started, should be low-key. Also, if exceptions are granted, we should grant licenses for all signed contracts in the U.S. and abroad for oil and gas equipment. U.S. industry would strongly object if we allowed exceptions only for one U.S. firm.

Decision: Grant exception by issuing export licenses for rotors after successfully negotiating with allies to take independent steps to block pipeline (withdrawal of loan guarantees)? /Note: Granting this exception means that we should examine -- with presumption of approval -- all signed contracts./

Yes_____ No_____